

STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 2001-289

June 5, 2001

NORTHERN UTILITIES, INC.,
Application for Approval to Issue Securities
to an Affiliate (\$60,000,000) (35-A M.R.S.A.
§§ 707, 901 & 902)

ORDER APPROVING
ISSUANCE OF
SECURITIES

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. SUMMARY

On April 25, 2001, Northern Utilities (NU or the Company) filed with this Commission a request for permission to issue an unsecured promissory note in an amount not to exceed \$60 million to an affiliated entity, NiSource Finance Corp. (NiSource Finance). The term of the note will not exceed 2 years and will bear interest at a rate of 5.75%. NU proposes to use the bulk of the proceeds to refinance existing long- and short-term debt with the remainder being reserved for future capital expenditures or gas purchases. This Order approves the Company's request.

II. DISCUSSION & DECISION

On March 20, 2001 in Docket No. 2001-101, the Commission approved the temporary extension to June 15, 2001 of an existing \$25 million revolving credit agreement between the Company and Fleet Bank. The purpose of that extension was to allow NU to explore a more permanent and cost effective alternative form of financing. At this time, the Company proposes to enter into a 2-year borrowing arrangement with its affiliate NiSource Finance for an amount not to exceed \$60 million at an annual interest rate of 5.75%. These proceeds will be used to retire the existing \$25 million revolving credit agreement as well as \$26.25 million in currently outstanding short-term debt. The remaining \$8.75 million will be used to fund future capital expenditures or gas purchases. The Company's capital budget for the 2001 calendar year is approximately \$8.4 million. The effect of this transaction on NU's balance sheet will be to reduce the common equity component of the Company's capital structure from approximately 61% to 58% (including short-term debt and current maturities of long-term debt). Based on recent industry data, we believe that a 58% common equity ratio is at the higher (and therefore safer) end of the spectrum for natural gas distribution companies today.

Due to the inter-company nature of this transaction, we must determine that the transaction including the 5.75% annual interest rate agreed upon by NU and NiSource Finance, is not adverse to the public interest. In response to a question from our Staff, the Company provided a table from the investment advisor A.G. Edwards that indicated that a gas utility with a Standard & Poor's rating of "BBB" could expect to issue long-term debt for 10 years at a spread (or "risk premium") of 170 to 175 basis points over a comparable treasury instrument. NiSource Finance and NU subsequently agreed to a spread of 155 basis points over a 2-year Treasury Note, which happened to be the same spread obtained by NiSource Finance on its own 2-year issuance in April 2001. Since NU and NiSource Finance reached the proposed agreement, the yield on 2-year Treasury Notes has increased somewhat, reducing the NU's spread to roughly 88 basis points (5.75% - 4.87% per the Federal Reserve's May 29, 2001 H.15 Release). In addition to a relatively favorable borrowing rate, Company witness Keane anticipates closing costs of roughly \$5,000 as opposed to an estimated \$100,000 for an "arms-length" third-party transaction.

We note one area of concern with this agreement. In our order approving the NiSource/Columbia merger, we specified that we would act to ensure that ratepayers would not be harmed in the way of higher rates following this merger. See *Northern Utilities, Inc., Request for Approval of Reorganization: Merger and Related Transaction*, Docket No. 2000-322, Order (Order) at 9. The NiSource/Columbia merger does have the potential to harm ratepayers specifically as it relates to this agreement. Prior to the NiSource/Columbia merger, Bay State had higher bond and commercial paper ratings than did NiSource. Following the merger, Bay States' ratings were lowered to be on par with those of NiSource, apparently due to the fact that NiSource significantly leveraged its balance sheet to fund the Columbia merger. This means that, at least in the near term, NU's interest expenses may be higher than they would have been but for the merger, which would be adverse to the public interest and thus would dissuade us from approving the proposed agreement.

There are, however, mitigating circumstances that convince us not to make such a finding. First, NU has not had a rate case in many years and therefore the cost of debt associated with this agreement is not actually in the Company's rates today and will not go into rates until after a rate case, if approved. Second, as stated in our order approving the NiSource/Columbia merger, the Company will have the burden of proof in showing that higher borrowing rates resulting from credit rating downgrades were not caused by the merger if it seeks to recover these higher costs in the future. Order at 9. Finally, an approval of the current request is subject to the usual reminder that it will not in any way limit the ability of the Commission to set the rates or charges of the Company in a future rate proceeding. Therefore, we conclude that the proposed arrangement is not adverse to the public interest and approve NU's request.

Accordingly, we

O R D E R

That Northern Utilities may issues its promissory note in an amount not to exceed \$60 million for a term not to exceed 2 years at a rate not to exceed 5.75%, to its affiliate NiSource Finance, as described in its filing of April 25, 2001.

Dated at Augusta, Maine, this 5th day of June, 2001.

BY ORDER OF THE COMMISSION

Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR:

Nugent
Diamond

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.
2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Appellate Procedure.
3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.